value balancing alliance

Position Paper on Standardization of disclosure requirements

As Value Balancing Alliance (VBA) we represent international companies with the ambition to integrate sustainability into the accounting and reporting ecosystems for improved decision making and capital allocation. Our goal is to enable stakeholders to compare the non-financial performance of companies like financial performance today.

Areas of further development

We fully support the current movement at standard setters (e.g., IFRS working group to accelerate convergence in global sustainability reporting standards) and policy makers (e.g., EU Commission) towards comprehensive reporting standards and taxonomies. In the following areas we see the main need for further development:

1. Harmonization and standardization: We strongly recommend that standard setters and policy makers harmonize disclosure requirements based on a building blocks approach starting with a globally accepted sustainability reporting foundation.
2. Data availability and robustness: We encourage policy makers to align the structure of taxonomies (based on "business activity" level) with effective and accepted accounting and reporting structures ("legal entity") to reduce implementation costs. Additional efforts are needed to increase the availability, robustness, and quality of non-financial data.[1]
3. Disclosure requirements and timelines: We strongly ask standard setters and policy makers to provide clear and consistent standards for disclosures at global level to avoid competitive disadvantages and grant companies sufficient time to prepare for disclosure.
4. Practitioners' perspective on feasibility and benefits: We recommend policy makers and standard setters to systematically engage again with practitioners from data providers and users to understand the feasibility of draft standards, the benefits of disclosures, and already existing and tested solutions.
5. Branding as "brown sectors": We call on policy makers to improve the communication that the taxonomies should not exclude specific sectors from access to capital. We already recognize first signs that financial market actors are more reluctant to provide capital to sectors affected by taxonomies. But here the highest investments in innovative technologies and business models are necessary for the sustainable transition.

[1] The piloting exercises within the VBA show that significant efforts are needed to increase data availability, robustness, and quality.

The (potential) role of the Value Balancing Alliance

As practitioners' lab, VBA members are testing and showcasing new accounting methods along the concept of double materiality. We are mandated by the EU Commission to develop a methodology promoting standardized natural capital accounting for businesses and are member of the EU Platform Sustainable Finance. We are cooperating closely with organizations such as OECD, IFRS Foundation, WEF, WBCSD, Capitals Coalition and others.

Based on our road-testing exercises and willingness of our members to support the creation of a global level playing field, we offer to share our methods and insights with policy makers and standard setters to enable a pragmatic, effective, and reasonable implementation of standards and legislation around non-financial reporting.

Specific comments on the role and solutions of the Value Balancing Alliance

As non-profit organization VBA brings together international companies from various sectors and regions. Our ambition is to integrate sustainability in accounting systems for more improved decision making and disclosures. A precondition is to change the way how company performance is measured and valued. For this purpose, VBA:

- Develops methodologies along the double materiality concept to support the standardization of future of accounting and reporting systems integrating natural, social, and human capital, governance, and additional intangibles.
- Members pilot the methodology in day-to-day applications to test feasibility and connectivity to existing systems. In peer learning and best practice sessions, our members exchange learnings and implications for decision-making and steering and to inform the further development of the methodology.
- Shares its insights with relevant organizations via its mandates (e.g., EU Platform Sustainable Finance, EU Transparent, OECD B4IG program) and network (e.g., IFRS Foundation, SASB, IIRC, WEF, WBCSD, Capitals Coalition, academic institutions etc.). and reaches out to SME to ensure midterm scalability of the methodology.

We strongly request standard setters and policy makers to take the VBA methodology[2] into account to build the foundation for disclosure requirements. It is one of the rare, if not the only, in day-to-day business tested methodology. It can be integrated in current performance reporting schemes and covers the double materiality concept in a structured way. Unlike other concepts, it takes business impacts along the value chain into account as well as the enterprise value. Therefore, the VBA methodology provides consistent and comparable data for management accounting and external disclosure.

[2] https://www.value-balancing.com/en/our-work.html

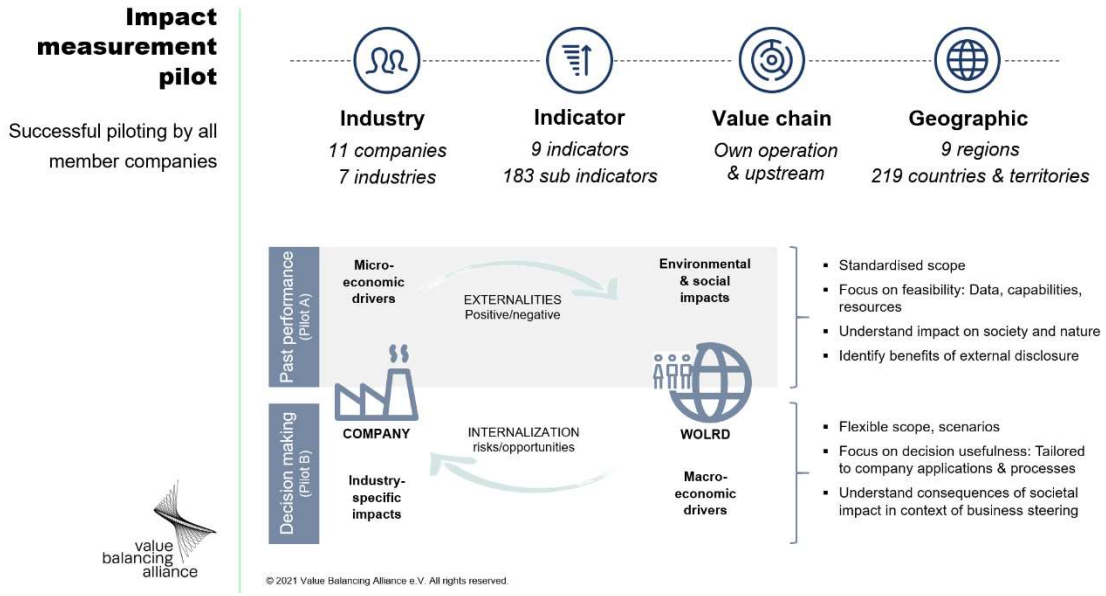

Figure 1: Overview of first phase of piloting

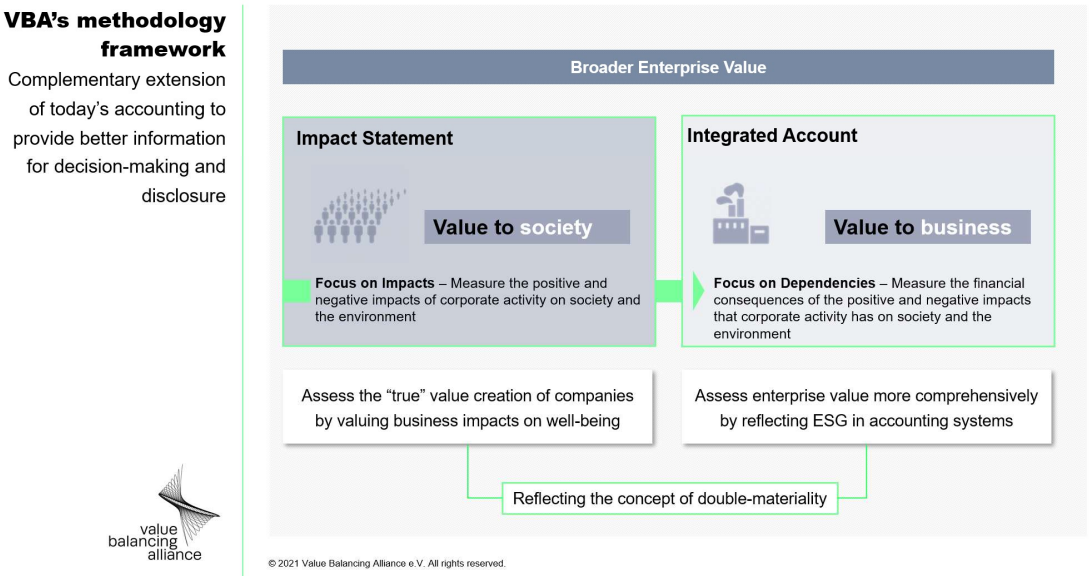

Figure 2: VBA Methodology along the double materiality

Specific comments on the development areas

Ad 1.: Harmonization and standardization

As globally operating companies, we support the development of harmonizing disclosure standards (e.g., formation of the Value Reporting Foundation, IFRS efforts to create non-financial reporting standards via a Sustainability Standards Board, double materiality concept, sector-specific standards) and taxonomies (e.g., objectives of the International Sustainable Finance Platform[3], and the announcement of Le Maire and Kerry of a joint working group on green finance and taxonomy[4]).

We ask standard setters and policy makers, as outlined by the IFRS Foundation, to harmonize regulation based on the building blocks approach, starting with a globally consistent foundation, and on existing frameworks (e.g., IFRS, GRI, SASB, IIRC, TCFD). Any other path forward would challenge the great achievements we made until today and changing the established basis would generate additional efforts and costs for companies.

In specific, **we strongly recommend** that the EU acts as driving force to develop global disclosure requirements but does not introduce EU specific standards before the structure of a global approach is established. The current focus on climate needs to take frameworks such as the TCFD into account.

Disclosure on climate can only be a starting point: To achieve a sustainable and inclusive economy, additional ESG value drivers need to be taken into account such as natural, social, and human capital, governance, or intangibles. To enable a holistic evaluation of a company's value contribution, as outlined by the EU Directive on Sustainability Disclosures, disclosures on the value to society (impacts) and the value to business (dependencies) need to be disclosed. To allow for comparability, while ensuring consistency, this will be done through two separate statements.

Ad 2.: Data availability and robustness

Regarding data availability, we see several challenges for the implementation of global disclosure standards.

- **Comparability**: For the time being, disclosure requirements and related metrics are not yet standardized. Therefore, companies are collecting different data for the various indicators and a meaningful comparison of results is not possible. A few initiatives, including the VBA, are working on the harmonization of sustainability accounting to enable a more consistent, comparable, robust, and

[3]https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/international-platform-sustainable-finance-annual-report-2020_en.pdf
[4] https://www.euractiv.com/section/energy-environment/news/france-proposes-common-us-eu-rules-for-green-finance/

ensured data base. A first questionnaire among the experts of VBA member companies has shown, that data robustness needs to be significantly improved.

We ask standard setters and policy makers to support the harmonization of sustainability accounting as solid foundation for disclosure, while providing sufficient time for companies to increase the robustness of data.

- **Structures**: Accounting and reporting data collection is currently structured along legal entities. Taxonomies, esp. the EU Taxonomy, strive for an additional layer: Business activities across legal entities. Most companies do not have this data available and respective IT-systems are not yet in place. This additional structure will increase the complexity for companies and create additional costs – not just in the set-up phase, also operating these systems next to the traditional accounts.

  We strongly recommend standard setters and policy makers to stay consistent with established structures and definition (e.g., IFRS) definitions and only where material, reasonable, and beneficial for users and providers, and efficiently implementable to add further structures for data collection.

- **Level of granularity**: As VBA we are convinced that a surpassing ESG or sustainability performance is a competitive advantage for companies against their peers, if towards customers, consumer, and investors. Therefore, we fully support the need for greater transparency and comparability in these areas. We are concerned that in a global market economy inconsistent disclosure requirement between countries and regions combined with the request to disclose too granular data (e.g., EU Taxonomy) will fundamentally challenge the competitiveness of companies. Compared to their competitors in other countries, companies would have high efforts and costs to meet additional disclosure requirements and providing business sensitive data demonstrating future investments and business strategies.

  We strongly request standard setters and policy makers to establish a globally effective level playing field and avoid requesting the disclosure of business sensitive data in the system of a market economy.

Ad 3.: Disclosure requirements and timelines

Taking the development at international, regional, and national level regarding reporting standards and taxonomies into account, we are concerned that diverging disclosure requirements will be imposed on companies. This would not only create additional efforts and costs, but also uncertainties and disorientation about the relevance of information. Looking at the timelines for the introduction of the EU Directive on Sustainability Disclosures and in specific the EU taxonomy, the timelines will pose unreasonable pressure on companies to establish new IT systems and adapt reporting structures. Under

the taxonomy, companies might be requested to report in 2022 for the reporting period 2021 about KPI for more than 70 business activities – and the criteria are not yet finalized.

We strongly recommend standard setters and policy makers to work towards a globally consistent disclosure framework and to build on standards and data structures which are already established. In addition, companies need a reasonable time to adjust their IT systems, build the respective tools and know-how for performance measurement and data collection and getting prepared for respective external assurance. Therefore, we strongly recommend a one-to-two-year testing period for all standards to understand the efforts and requirements in detail.

Ad 4.: Practitioners' perspective on feasibility and benefits

The movement towards disclosure standards and regulation is at different levels of maturity, pace, and direction. Impacted organizations, esp. data preparers and users, have gained tremendous insights and knowledge about the potential implications over the last months. They have also started to collaborate across industries to provide pragmatic business solutions for the various challenges, such as in the VBA.

We ask standard setters and policy makers to take this additional knowledge into account and systematically reach out to companies, the data preparers, and data users (i.e., investors). Data preparers urgently need to understand the feasibility of upcoming disclosure requirements as well as the benefits for users. The consultation should take place after standards have been finalized for meaningful testing. A one-to-two-year period will be required to provide robust feedback and inform a further development of regulation. We also recommend strongly to compare already existing and tested frameworks in the market to deliver on the disclosure requirements.

Ad 5.: Branding as "brown" sectors

Classification systems such as the EU taxonomy intend to provide guidance which business activities and models are sustainable. The challenge is that non-sustainable business models have the highest leverage to achieve sustainable economies (e.g., extractives, energy, transportation). However, we already recognize that access to capital to enable the transition is reduced due to the labelling as "brown".

We ask policy makers to change the communication using symbolic terms as "brown" and intensify the outreach to relevant stakeholders, mainly financial market players, to enhance the understanding of a classification system. A limited access to capital for sectors with the biggest sustainability challenges might become a roadblock for the transition towards a sustainable and inclusive economy.